

BUSINESS CONDITIONS

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Recent Money Market Developments

Member Bank Accounts Reflect Treasury Operations

Bank investment and deposit changes in the first three months of 1946 represented a marked departure from the familiar pattern which characterized the war period. Accounts of weekly reporting member banks showed only a minor shift from Government war loan accounts to private deposits during January, while in February this relationship was actually reversed, and in March both classes of deposits were reduced. Government security holdings expanded to a peak of 49.7 billion dollars on February 7 and were maintained at high levels until the March redemptions.

The failure of demand deposits adjusted to expand after the Victory Loan Drive is attributable to lower Government expenditures, withdrawals for income tax payments, and heavy purchases of Government securities by the public, particularly the restricted issues. Proceeds from the redemption of securities held by nonbank investors were also used to purchase outstanding Governments rather than to expand deposits. The strong demand for Governments which developed early in the year reflected both uncertainty as to the future of interest rates and the prospect, in view of the Treasury's large cash balance, that no issues for new money would be forthcoming in the near future.

While required reserves remained relatively stable, member banks gained reserves through the return flow of gold to the United States and through a 650 million-dollar reduction in currency in circulation during the first three months of the year. These factors, however, were far outweighed by the temporary growth of Treasury deposits at the Reserve Banks during the latter part of March and by a large net reduction in Reserve Bank credit. As a result, reserve balances and excess reserves declined more than 500 million dollars for the period as a whole.

The 900 million-dollar reduction in Reserve Bank credit between January 2 and March 27 reflected heavy demands by the banks for certificates which were supplied by the Reserve Banks. In part, these demands developed as banks undertook to replace securities redeemed or scheduled for redemption in cash. Certificates held by reporting member banks rose 934 million dollars from December 26 through February 20 but declined subsequently as a result of cash redemptions of certificates in March and sales of certificates as tax payments and war loan withdrawals tightened the reserve positions of these banks. Because of sustained demand for certificates by non-reporting banks and others, however, Reserve Bank holdings did not reverse their downward trend until after March 20. The net reduction in certificates held by the Reserve Banks amounted to more than 2 billion dollars during the first three months of the year.

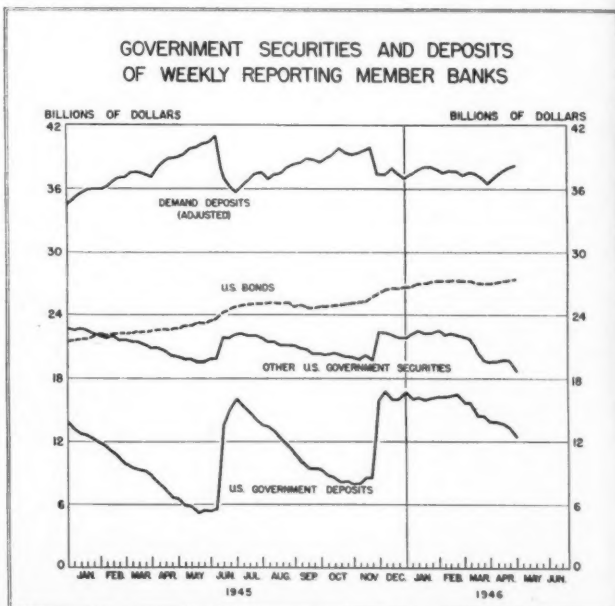
Meanwhile, System holdings of Treasury bills rose 1 billion dollars to a record high of 13.7 billions on March 27. Bill holdings of reporting banks in New York declined to 111 million dollars on March 27, the lowest level since early

in 1939. Discounts and advances by the Reserve Banks also showed sizable increases.

Total member bank reserve balances were not greatly affected by the March cash redemptions. Since the largest proportion of the redeemed securities was held by commercial banks, the effect of cash payment of these securities was largely to reduce both war loan deposits and earning assets.

Member bank reserve positions were temporarily eased as a result of the cash redemptions of certificates on April 1 and May 1. The Treasury redeemed in cash 2 billion dollars of certificates maturing on April 1, and reduced its balance with the Reserve Banks by about 1 billion dollars. Part of these funds were absorbed through redemption of maturing certificates held by Reserve Banks and the remainder went into bank reserves. Member banks used a part of these funds to retire Federal Reserve credit outstanding, principally through repurchases of Treasury bills. Member bank reserves were expanded through the cash redemption operations on May 1, reductions in Treasury and nonmember balances and sales of bills to the System offsetting the effects of the decline in Reserve Bank credit which resulted from the redemption of over 350 million of certificates held by the Reserve Banks.

Certificates held by the weekly reporting member banks declined 1.3 billion dollars from March 27 through May 1, while those held by the Reserve Banks dropped an additional 800 million dollars. Reporting banks continued to purchase Government securities in the market, and increased their holdings by about 400 million during this period.



Confusion Rules Dairy Situation

Complexities Continue to Puzzle the Industry

The current dairy situation continues to present one of the thorniest problems in national food administration. Shifts in the prewar pattern of milk uses enforced by regulations and rationing have created major problems of readjustment as the controls relaxed. One outstanding feature of these readjustments has been the decline in butter production. In the face of what has been characterized as unprecedented demand for butter, the total production during 1946 has been running 25 to 30 per cent below the low level of production prevailing in 1945.

Creameries have been forced to close, and the complaint of those associated with the butter industry is that this unnatural development is due to errors of price administration. Specifically it is contended that the ceilings on butter are too low and make it impossible for butter producers to obtain the supplies of butterfat which the market would absorb if ceiling prices on butter were eliminated, or raised relative to the prices currently being paid for other dairy products. It is charged that the absence of price ceilings on cream for fluid sale and for use in ice cream and other food products has resulted in prices on cream being high enough to divert cream away from butter production.

WAR NEEDS FORCED SHIFTS AND CONTROLS

The wartime requirements for food necessitated substantial changes in the utilization of milk so extreme that the "normal" pattern was materially disrupted. The needs of the military forces and of lend-lease aid to the Allies had to be met with products which could be processed so as to keep for a long time and to economize on shipping space.

Another consideration making for shifts in the dairy industry was the fact that with the tremendously stepped up demand for foods it was deemed sound policy to encourage the maximum use of all the nutrients contained in whole milk. The consequence of these two considerations was a very material increase in the production of such foods as cheese and dried and evaporated milk.

When price controls were instituted, ceilings were put on some dairy products such as butter, cheese, fluid whole milk, and evaporated and condensed milk; but it was felt at that time that ceilings on fluid cream would be impractical of administration. In order to achieve the optimum desired utilization of milk products the whole list of milk and dairy products were, during 1943 and 1944, put under restrictive regulation of one form or another.

Butter was subjected to set-aside orders for Government purchase. Similar requirements were made with respect to cheddar cheese and non-fat dried milk solids. The sale of fluid cream containing more than 19 per cent butterfat was prohibited. The use of milk solids in frozen dairy foods was put under limitation. Production of cheese other than

cheddar was restricted. For fluid milk and cream, sales areas were established, base periods were assigned, and quotas were set up limiting sales. Following the end of the war in August practically all of these controls were terminated or suspended. With the removal of these restrictions milk was free to move more easily into the different products and uses in line with the existing price relationships, some of which remained under price control.

To stimulate additional production of milk, higher returns to producers were thought necessary. In lieu of price ceiling increases, subsidies were paid on butter and cheese. A "dairy production payments program" was instituted, payable directly to eligible farmers to cover increased labor, feed, and other costs. The payments varied by regions and throughout the seasons, the latter provision being designed to encourage the production of milk during the fall and winter months when it is normally lowest. The butter and cheese subsidies have been eliminated and price ceilings raised to compensate, but the dairy payments program is scheduled to continue through the current and coming seasons.

Beginning in early 1943 a program of subsidies on fluid milk was instituted for milk distributors operating in 13 important fluid milk markets. The rates ranged generally from 20 to 40 cents per cwt., determined largely by the extent to which returns to milk producers would otherwise have been reduced. The object of this program was to permit milk distributors to pay higher prices to producers without requiring higher ceilings or higher prices to consumers to be established by the OPA. This program also was a recognition of the increasing farm labor and other costs in producing milk and of the competitively attractive alternative lines of farm production.

The importance of the subsidies paid on milk and dairy products is indicated by the fact that in 1945 such subsidies constituted nearly one-sixth of the total returns to producers on the milk and butterfat sold. The dairy production payments program, payments made directly to farmers, alone accounted for most of these subsidies, amounting to nearly 14 per cent of the total returns to farmers.

PRODUCTION SHIFTS

The total production of milk on the nation's farms expanded substantially during the war years. During the five prewar years the average production was 105 billion pounds. For each of the three years, 1942-44, production was 118 to 119 billion pounds. Last year all records were broken with an output of over 122 billion pounds. It is expected that 1946 production will show a very material decline below this figure, variously estimated at 3 to 7 or 8 per cent. With rising labor wages paid to farm hands and with increasing

scarcities of feed, some farmers are reported to be reducing their dairy herds, either in whole or in part.

A study made in the spring of 1942 indicates that families with intermediate incomes consume about 50 per cent more dairy products per person than do families with low incomes. But the differences in consumption are much greater for some products than for others. The intermediate income families appear to spend about six times as much for cream as do the low income families, four to five times as much for ice cream, twice as much for cheese, and 50 per cent more for butter and fluid milk.

The combination of Government limitations on product use, price and subsidy programs, and the changing demand resulted in expanded production of milk and in marked shifts in the utilization of milk in different products. In the five prewar years, 1936-40, 31 per cent of the total farm production of milk was consumed in fluid milk or cream. For 1945 over 38 per cent of milk production was consumed in this manner. In the prewar years only 5 per cent of the milk went into the production of American cheese, whereas for the last year over 7 per cent was utilized for cheese. Evaporated milk absorbed a little over 4 per cent in the years before the war, while last year it accounted for nearly 7 per cent of the total. The proportion utilized for ice cream production increased from 3.2 per cent before the war to 4 per cent of the total milk produced in 1945.

Creamery butter utilized nearly one-third of the total farm milk production in the five prewar years, while currently only about one-fifth of the total milk produced is going into creamery butter. An examination of the production trends during the war reveals that butter was the only dairy product to decline during the war years.

The production of creamery butter totaled 1,872 million pounds in 1941. For last year, production is estimated to have been 1,370 million pounds. After deducting Government requirements, the per capita consumption by the civilian population was about 14 pounds in 1941 as against 8 pounds last year. The American Butter Institute estimates that only 900 million pounds will be produced in 1946 if the present trends in total milk production and utilization continue, and that after allowing for Government requirements and the increase in population, the civilian per capita consumption will be about 6 pounds.

These figures do not include the civilian consumption of farm-churned butter amounting to about 3 pounds per capita. Consideration of table fat consumption should also include mention of oleomargarine. In prewar years the average consumption was just over 2 pounds per person. Currently the rate is over 4 pounds.

Creamery butter production in 1945 was more than 20 per cent below the 1936-40 average. American cheese output last year was more than 60 per cent above the prewar average, and output of other types of cheese was nearly 50 per cent above prewar. In the case of evaporated milk, 1945 production was more than three-fourths above prewar. The output of ice cream was nearly doubled. While still a relatively small factor in the dairy products picture, dried whole milk was expanded more than ten-fold during the war. The consumption of fluid milk and cream expanded

by 50 per cent.

ARE PRICES OUT OF LINE?

With the end of most of the limitations, regulations, and rationing during the latter part of 1945, milk has been shifting again into uses according to relative prices. There have been large increases in the use of milk in the form of fluid milk, cream, and ice cream. During the last quarter of 1945 uses of milk for ice cream and fluid cream were more than 40 per cent above the last quarter of 1944, and the consumption of fluid milk was up by 6 per cent. These increases were made at the expense of butter, cheese, and evaporated milk, consumption of which had declined by 19, 5, and 19 per cent respectively. These very substantial shifts fell with terrific impact upon the processing and distributing industries which normally manufactured or distributed butter, evaporated milk, and cheese. Representatives of these industries have repeatedly urged price adjustments upward which would permit them to obtain a larger proportional share of the total milk supply to manufacture their products.

One of the charges that has been made with regard to the price administration of dairy products is that because of the price ceiling on butter this product is suffering a relative price disadvantage. It is difficult to support this contention on the basis of wholesale market prices. The wholesale prices of milk and other dairy products, on the basis of representative market quotations, are currently 55 per cent above the 1936-40 level. This measurement is derived by weighting the various products according to proportionate production of each. On such a basis the prices of both butter and cheese are in relatively favorable positions to what they were in the prewar years. Evaporated milk and fluid milk and cream appear to be in a relatively disadvantageous position. The Chicago wholesale price of 92-score butter during 1945 and currently is 57 per cent above the prewar average. The wholesale price of American twins, Wisconsin cheese, is 90 per cent above prewar. Evaporated milk (the wholesale price of manufacturers) is only 44 per cent above prewar, while the wholesale price of 40 per cent cream at New York is up 49 per cent, and the wholesale price of fluid whole milk in principal cities is 48 per cent above the prewar averages. From this it would appear that if the five prewar years be taken as a basis for normal relationships between the prices of the various dairy products, American cheese is currently in the most advantaged position, butter is only very slightly above the relative level for all dairy products taken together, while evaporated milk and fluid milk and cream are 4 to 7 per cent below the current level for dairy products as a whole.

In spite of the apparently greater relative increase in the price of butter than in the price for cream, the volume of cream utilized for creamery butter manufacture has declined while the volume used for fluid consumption has been increasing materially. A partial explanation of this shift may lie in the fact that the actual value of butterfat in cream sold at wholesale in the principal cream markets has risen more than the price received by farmers for

butterfat sold. In other words, current margins between these two prices are larger than normal. While this might tend to encourage the utilization of more cream for fluid consumption and less for manufacturing butter, the extent of the increase in the differential appears inadequate to explain the shifts in utilization that have taken place as to the two uses. In other words, a readjustment of butter prices that would re-establish the differentials prevailing before the war would not appear sufficient to divert enough cream to the making of butter to re-establish the normal proportionate relationships prevailing before the war.

OTHER FACTORS THAN PRICES IMPORTANT

Perhaps a partial explanation lies in the fact that larger incomes are in the hands of civilian consumers. It has already been shown from the figures cited on consumption by different income classes that as incomes rise, consumers tend to expand their consumption of fluid cream, ice cream, and cheese much more than they do their consumption of butter and fluid milk. Such indications, however, cannot possibly be twisted to justify an actual reduction in butter consumption. But the operation of these tendencies as to incomes would help to explain the increased consumption of fluid cream and ice cream, both of which were rather drastically curtailed during the latter part of the war years. In this sense it would appear unnatural to expect the same utilization of milk into these products during a high income period that prevailed during a more "normal" period when average incomes were lower. It would appear that such a "normal" utilization would require relatively higher prices for cream relative to butter than prevail at the present time.

Another partial explanation of the existing situation may lie in the fact that farmers, in order to satisfy the wartime demands for dried non-fat milk solids, shifted from the sale of farm-separated cream to the sale of whole milk. This is a shift which many farmers were desirous of making in more normal times because it is commonly believed among dairy farmers that a whole-milk market outlet is more profitable than the sale of cream alone. As a result of this shift more cream was available upon which a choice could be made between manufacture into butter, use in other manufactured dairy products, or sale as fluid cream. While not all of such cream was of a quality to move readily as fluid cream, much of it found ready markets in many areas, especially in view of the "thirst" for cream, resulting from wartime restrictions, to which reference has already been made. When in addition to this factor it is remembered that there was a wartime growth of population in urban centers and that to some extent such centers of population reached out farther and farther for fluid milk supplies, it is not surprising that the shift away from farm separation of cream to the sale of whole milk has put the butter manufacturing industry to some extent in a position of disadvantage.

During 1945 there was a decrease of 3 per cent in the number of milk cows on farms in the nation. According to current indications this decrease has continued during 1946. This decrease in numbers has tended to curtail milk pro-

duction in recent months. However, the decreases in dairy cows have been relatively much greater in the west north central states in which milk is sold primarily for manufacture into butter. This has tended to decrease butter production relative to the production of other dairy products. The areas reporting greatest decreases in milk cows also reported the greatest increases in hog numbers, thus indicating the increasing competition of hogs for the scarce feed and expensive labor on the farms in these areas. Labor requirements for dairy herds are large relative to some other farm enterprises, particularly hogs. Farm wage rates have increased relatively more in recent years in the west north central states than in any other region.

The problem of restoring "normal" relationships in the dairy industry is like many other problems of adjusting to peacetime conditions. Public officials are apparently caught up on the horns of the dilemma of continuing to fight inflation on the one hand and to permit free economic interplay on the other. A large segment of the dairy industry asks the removal of all controls and ceilings to permit "supply and demand" to establish the relationships between different dairy products as to utilization and price. Most dairy farmers want all subsidies and price ceilings removed. The enterprises associated with the manufacturing and distribution of some products, particularly butter, ask for the removal of price ceilings or a higher ceiling for butter. Defenders of price control as a weapon against inflation contend, upon the other hand, that given the present level of consumer demand the removal of all controls would result in a dangerous increase in the total cost of food to the consumer. It is further argued that to permit substantial price increases at this time would be unfair to those consumers who have gone through the war period without the relative increase in incomes enjoyed by some of the people. This is an argument against inflation, and it can with equal force be said that someone is always "unfairly" treated whenever the price of any commodity rises.

At the present time dairy farmers are reported to be discouraged with the price prospects for the coming year. The current Government program for dealing with the dairy situation, which has been announced but not yet implemented, calls for relatively larger subsidy payments under the dairy payments program and for a reinstatement of the limitations on the uses of milk in ice cream and on fluid cream, with an outright prohibition of the sale of whipping cream. It is also proposed to establish for the first time ceiling prices on the sale of commercially separated cream and on the resale of farm-separated cream.

It appears that the price of butter is not greatly out of line with other dairy products. An increase in the price of butter might temporarily divert some milk and cream to butter manufacture, but it is probable that the net result would be to boost the prices for dairy products generally, without much permanent increase in the proportion of milk and cream going into butter. While such a change would doubtless encourage dairy farmers to remain in maximum production, it would be in conflict with the determination to hold food prices in check, which seems to continue as official policy.

Seventh District Coal Crisis

Bituminous Strike Causes Temporary Economic Paralysis

Lack of coal, attributable to one of the most far-reaching strikes in the nation's history, in May paralyzed much of the economic life of the Seventh Federal Reserve District, already severely hit since V-J Day by continual work stoppages and related production delays. In contrast to most other Districts which economically are able to make more extensive use of fuels other than bituminous coal, the Seventh District, comprising most of Illinois, Indiana, Michigan, and Wisconsin and all of Iowa, depends almost entirely upon coal for industrial and domestic fuel uses.

With 15 per cent of the nation's population, the Seventh District consumes more than 25 per cent of the bituminous coal used in the nation, but produces only 5 per cent. Coal is not only the District's most important source of power but also a key raw material for many phases of industrial production, notably steel and chemicals.

The primary effects of the coal shortage began to appear shortly after the outbreak of the United Mine Workers (A.F.L.) strike on April 1 when bituminous coal production in the nation dropped to about five per cent of its pre-strike rate. The situation became acute in this District following the strike on April 30 of the independent Progressive Mine Workers who accounted for the remaining coal production, of vital importance to the Seventh District. Almost immediate effects were drastically curtailed operations by steel plants, railroads, and to a somewhat lesser extent by utilities. Illustrative of the basic dependency of the District upon coal and of industries upon each other, secondary effects of the coal crisis have permeated virtually all phases of the District's economic life.

The short-run outlook for Seventh District industry and commerce continues to be pessimistic in contrast to previous expectations because, although coal production was temporarily resumed by union authorization on May 10, consumption of this coal has been necessarily limited to uses essential to public health and safety. Consequently, non-utility industrial and commercial coal inventories continue to be gravely depleted where they have not already been exhausted. When full coal production is resumed, moreover, from one to two weeks at least will be required before the newly mined coal will reach many primary consumers.

Although the Seventh Federal Reserve District produces comparatively little coal, about 45 per cent of its coal requirements are mined within the five District states, principally in the downstate areas of Illinois and Indiana which lie in the Eighth Federal Reserve District and which form the principal center of strength of the Progressive Mine Workers Union. Most of the remaining 55 per cent of the coal consumed in the District is received from the more distant Appalachian fields.

During the peak of wartime production in 1944, more than 160 million tons of bituminous coal and lignite were

consumed by all users in the Seventh District states. Industrial firms are by far the most important consumers of soft coal in this District, accounting for approximately 75 per cent of total consumption. Railroads require more than one-fourth and utilities burn somewhat less than a sixth of the industrial coal consumed, with the remaining coal tonnage largely used by manufacturing and commercial establishments. Although coal requirements for industrial production since V-J Day have been somewhat less than during the war, the necessary volume of tonnage is still well above prewar requirements.

Soft coal is the predominate fuel used for residential heating in the Seventh District. More than 75 per cent of the District's dwellings are heated by bituminous coal or coke, as compared with only 40 per cent in the nation.

Although production of bituminous coal increased substantially during 1941-45, consumption also expanded at least to the same extent. Despite wartime conservation measures and the decline of some soft coal requirements following V-J Day, a continuing high level of consumption prevented any substantial stock-piling of coal. Immediate pre-strike inventories, consequently, on the average were not only seasonally low but as limited as at any time during the war emergency. Moreover, the situation was aggravated by uneven distribution of existing supplies.

In the Seventh District, as elsewhere, the coal strike had its most immediate and sharpest effects upon prime users of coal, resulting in loss of employment for at least 50,000 workers making basic iron and steel products and for thousands of others in railroads and coal by-product industries, in addition to more than 20,000 coal miners. As the strike continued, the number of workers adversely affected mounted at an increasing rate, so that after six weeks it is estimated that for varying periods of time the employment of more than half of all manufacturing workers and probably at least a fifth of non-manufacturing workers in the District had been completely or partially interrupted because of fuel and power shortages and the related transportation embargo.

Within the Seventh District, the Chicago industrial area has been most severely hit by the coal shortage because of a greater-than-average dependency upon coal, more depleted pre-strike inventories, and near "hand-to-mouth" reliance upon downstate Illinois-Indiana coal supplies for major utilities. Dim-out restrictions upon the use of power limited electric consumption by industrial and commercial firms to 24 hours per week. All other District industrial areas were affected by coal and related material shortages, but power restrictions generally were voluntary and less severe than in Chicago. In almost all instances, however, more drastic conservation measures were about to be undertaken when the strike "truce" became effective.

Federal Aid for Public Airports

500 Million Dollars of Grants Authorized for Seven-Year Program

The Federal Airport Act, approved by President Truman on May 13, 1946, establishes a Federal policy toward the financing of terminal facilities for commercial and private flying which will keep ownership and operation of air fields by the Federal Government at a minimum but will offer substantial inducements to states and municipalities to provide these facilities. In its broad outline the policy contained in this Act is a logical outgrowth of the Federal interest and contribution to developments in airport finance and ownership during the past two decades. Twenty years ago the Air Commerce Act of 1926 excluded ownership, operation, and maintenance of airports from an authorization to the Secretary of Commerce to establish and operate air navigation facilities. The policy of leaving airport ownership and operation in private hands or to state or municipal authorities was amended by the Civil Aeronautics Act of 1938 by permitting the Administrator of Civil Aeronautics to establish, construct, or operate airports but prohibiting the Administrator from acquiring any airport by purchase or condemnation. Under this authority the Civil Aeronautics Authority leased and developed the C.A.A. Intermediate fields as essential facilities for air commerce.

The Federal Airport Act is designed to promote the development of a nationwide system of airports capable of serving the needs of civil aviation by encouraging state and local governments to acquire or construct new ports or to enlarge and improve those they already own. Federal funds will be available on a matching basis for investment in facilities that fit into the National Airport Plan to be developed by the Civil Aeronautics Administration. Authorization for appropriations aggregating 500 million dollars over a seven-year period are provided. After allowance for the Administrator's planning program and administration costs, 118.8 million dollars is set aside as a discretionary grant fund. The remaining 356.3 million dollars is allocated among the states by a statutory formula based on area and population. The total seven-year allocation to the Seventh District states under the formula is 45.8 million dollars; the Illinois share is 14.1 million dollars; Indiana, 6.8 million

dollars; Iowa, 6.8 million dollars; Michigan, 10.6 million dollars; and Wisconsin, 7.6 million dollars. The amount to be spent in any one of these states may be increased by grants to the extent that the Administrator deems a larger expenditure in that state is essential to the national airport plan and if matching funds are locally available.

AIRPORT DEVELOPMENT

In the past twenty years the interest of several Federal agencies in aviation development has been a major factor in airport expansion, but financial aid has been a by-product or incidental to other purposes. Shortly after World War I, when airmail service was initiated, the Post Office Department was active in promoting airport development. The Army in these early years also stimulated interest in civil aviation. Federal financial assistance for civil airports, however, began with the emergency relief construction programs of the early and middle 1930's. The Civil Works Administration, the Federal Emergency Relief Administration, and the Public Works Administration spent approximately 32.5 million dollars for airport construction. The larger and better coordinated program of the Works Projects Administration involved expenditures of 331 million dollars up to the end of 1942.

None of these programs, however, bore the necessary relationship to a balanced and integrated plan of airport development calculated to cover aviation needs of the country. The need for military airport facilities at the beginning of World War II led to another era of substantial Federal expenditure. Here, again, the emphasis was on military needs and not on those of civil aviation; many of the fields built for wartime needs are of scant importance in peacetime. The Civil Aeronautics Administration, under whose direction the construction of national defense airports was carried out during the defense and war years, spent 331 million dollars for these facilities up to March 1, 1945.

Except for regular Army or Navy airports, intermediate emergency landing fields leased and operated by the Civil Aeronautics Administration, the Washington National Airport, and a small number of landing areas owned by such Federal agencies as the Park Service and Forest Service, the Federal Government neither owns nor operates airports.

Virtually all of the larger civil airports are owned by cities or counties or their instrumentalities; they are usually publicly operated, though private operation in whole or in part is a common practice. A large number of airfields suitable for private planes are owned and operated commercially or simply as private ports by one or a small group of plane owners. The character of airport ownership during the past twenty years is indicated in Table 1.

Exclusive of expenditures made directly by the War and

TABLE 1
AIRPORT OWNERSHIP IN THE UNITED STATES
1927-45

Type of Owner	Number of Airports				
	1927	1932	1937	1942	1945
Municipalities	414	717	990	1,129	979
Commercial	409	872	778	1,069	883
CAA Intermediate	134	352	283	273	242
Military, Private, & Misc.	79	101	158	338	982
Total	1,036	2,042	2,209	2,809	3,086

SOURCE: *Public Aids to Domestic Transportation*, (H. D. No. 159, 79th Congress, 1st Session), p. 485.

Navy Departments, the Federal Government has invested approximately 700 million dollars in airports up to the present time. Nearly half of this total was allocated to large airports used for commercial air transport. Up to 1941 the states made capital outlays for airports of nearly 13 million dollars and the localities of over 150 million dollars. At the end of 1945 state and local investment probably totals well over 300 million dollars, of which from two-thirds to three-fourths has been for the larger air terminals. Omitting the exclusively military, private, and commercial ports from consideration, the present airport system involves a gross investment of over one billion dollars. On account of the fact that military needs have dictated much of the Federal construction, that unemployment relief was a major purpose of Federal grants in the 1930's, and that the rapid technological changes in aircraft have altered terminal requirements, the billion-dollar investment overstates the reproduction cost of publicly owned airports suitable for civil aviation.

ACT REQUIRES NATIONAL AIRPORT PLAN

The Federal Airport Act charges the Administrator of Civil Aeronautics with the responsibility of formulating and annually revising a national plan for airport development. The plan must specify the general location of airports and the type of development suitable to each location. The facilities thus provided are reasonably to anticipate the needs of civil aviation including both air commerce and private flying. In the preparation of the plan, the Administrator is to consider technological changes and developments in aviation and to consult with the state authorities concerned with aviation, the Civil Aeronautics Board, the Federal Communications Commission, and the military services. While the primary objective is to provide for civil aviation, national defense considerations and aviation programs of the military services are to be taken into account. The initial costs of planning and research are to be met by an immediate appropriation of 3 million dollars to the Administrator and by succeeding appropriations of 3.5 million dollars or 5 per cent of the annual grants for airport acquisition and construction whichever is larger. This amount will cover administrative, planning, and research expenses of the Administrator. The planning of a national airport system and the administration of Federal aid, therefore, visualizes the expenditure of approximately 28 million dollars.

GRANTS TO STATES AND LOCAL GOVERNMENTS

Federal grants for airport construction are available only to public agencies; specifically, to states, counties, cities, villages, and other local governments, including such special-purpose units as airport authorities and governmental instrumentalities. A limited number of Federal agencies also may qualify. No provision is made for assistance to commercial or private ports, and a public agency must hold title to the site or give the Administrator sufficient assurance that such title will be acquired. The Act, however, contains no restrictions on the leasing of public ports to private operators; presumably, if a municipality so desired it could

obtain Federal funds to acquire a site, construct an airport, and lease the port to a private operator if other conditions were complied with.

Other conditions under which Federal funds are available relate to the project itself and to the operation of the field after the project has been completed. Federal monies are restricted to outlays necessary to development in conformance with plans developed from standards set by the Civil Aeronautics Administrator. These standards include such matters as site location, airport layout, grading, drainage, paving, lighting, and safety of approaches. Under these conditions a grant agreement can be entered into between the municipality and the Administrator. The Administrator, however, also is required to receive assurances in writing that the following conditions will be satisfied when the airport is placed in operation:

- (1) Facilities will be available for public use on fair and reasonable terms and without unjust discrimination,
- (2) The port and its facilities will be suitably operated and properly maintained,
- (3) Aerial approaches to the port will be cleared or protected by mitigating existing hazards and by prevention of future hazards through zoning,
- (4) Facilities are to be available for use of military and naval aircraft at all times without charge unless such use is substantial, in which case a reasonable proportion of the cost of operation and maintenance, based upon use, may be charged,
- (5) Space in airport buildings required by Federal authorities for air traffic and control, weather reporting, and communications activities related to traffic control shall be available without cost except for light, heat, and similar facilities, and
- (6) Financial accounts and records relating to the project shall be kept in accordance with the accounting system prescribed by the Administrator, and annual statements and special reports on operations shall be available to the Administrator.

Under these conditions the participating local government may receive a grant of up to 50 per cent of the cost of airport development undertaken subsequent to the enactment of the Federal Airport Act provided that the total of such grants including administrative costs may not exceed 100 million dollars in any one year. The total expenditure may include original construction, improvement, repair of the airport itself and the administration buildings, the removal or marking of hazards, the making of surveys and plans, and the acquisition of sites or rights to air space. The construction is specifically excluded.

The precise proportion of sharing depends upon the type of airport. The various classifications contemplated by the Act are shown in Table 2. For Class III and small airports, 50 per cent of the allowable costs is to be granted. For the larger airports the proportion may be as much as 50 per cent or it may be less, at the Administrator's discretion. The proportion may be increased up to as much as 25 per cent of the total cost in states—typically in the West—where there are large holdings of public lands or non-taxable Indian lands. In addition there is a restriction on aids for the por-

tion of airport costs for acquisition of site and interests in air space. The Federal share of these costs for smaller ports is 25 per cent, and, in the case of larger ports, may be less than 25 per cent, also at the discretion of the Administrator.

GRANTS FOLLOW FEDERAL AID PATTERN

The grant policy incorporated in the Airport Aid Act resembles with only two important differences the pattern of Federal aid to states for highway construction. The amounts available for expenditure are to be fixed by annual lump-sum appropriations of the Congress. (The Act itself appropriates no funds but merely provides a parliamentary authorization with specified limits for subsequent annual appropriations.) Three-fourths of these annual amounts, after the deduction of planning and administrative costs, are apportioned among the states by a statutory formula giving equal weight to population and area. At least 50 per cent matching is required from states and localities except in states where large areas of public lands are located; this modification is adapted from highway aid precedents. The section which permits the Civil Aeronautics Administrator to apportion 25 per cent of the annual grant to airports most urgently needed, regardless of their geographical location, does not affect matching requirements, but it does permit a different distribution among the states than would obtain if the entire fund were apportioned according to formula. This discretionary power was not provided for in the Federal Aid Highway Act which apportions the entire Federal grant by statutory formula.

To the extent that the 25 per cent discretionary allotment is apportioned to Class IV and V airports, each specific grant is subject to approval by the Congress. While the Act does not so require, it is likely that a large portion of the discretionary fund will be allotted to the larger airports. Indeed, one of the earlier versions of the Airport Aid Act specifically earmarked 35 per cent of total grants for the development of Class IV and V airports. Affording a Federal agency some range of discretion in allocation of grants is now a fairly common feature of the Federal grant policy; it permits greater flexibility in the over-all program than can

be attained by a complete reliance on a rigid formula.

The aid bill enacted by the House prohibited Federal aid for site acquisition. This restriction was removed in the Conference measure and, as enacted, Federal funds are available for any expenditure excepting hangars.

The other feature that distinguishes grant policy under the Federal Airport Act from the majority of Federal aid programs is the provision that the Civil Aeronautics Administrator may deal directly with municipalities and local governments instead of channeling all funds through a state agency. The precedents for this policy are limited. While Federal aid for highways often has ultimately been disbursed for local roads, funds have been channeled through state highway departments. During the 1930's, the Federal Government through the WPA and PWA entered into direct loan and grant negotiations with local governments, but this practice has not been incorporated into the typical, permanent grant-in-aid program. This particular feature of the Airport Act was vigorously contested in the Congress. The original House bill permitted the Federal Government to deal directly with the local units, while the Senate bill required all funds to be channeled through some state authority. The final compromise permits direct dealing between the Administrator and the localities excepting where a state forbids it by statutory enactment. The issue involves a deep-seated difference of opinion as to the proper intergovernmental relationships. The states, through the Council of State Governments, took the position that the Federal Government should at all times effect such policies as concern local units, with the states as intermediaries. The Conference of Mayors, on the other hand, contended that airport construction was a vital and direct concern of the cities, and, that since the states had evidenced little or no interest in such construction, a direct Federal-municipal relationship was preferable.

States have had only a casual interest in promoting and developing civil aviation and that their expenditures for terminal facilities have been a small fraction of those of municipalities or the Federal Government. Recently, however, state aviation departments and aeronautical commissions have been created in the majority of the states, and it is possible that state funds for airports will be forthcoming in the future. The cities and other local units of government, because of their limited revenue sources, are typically less able to provide funds for airports than the states with their relatively well-developed revenue systems. The greater part of large municipal expenditures for airports have come from bond issues serviced from property tax levies and from charges and rentals paid by users of such facilities. The states generally have not yet demonstrated their willingness or interest in making the financial contribution required for airport development. While a majority are now furnishing technical and advisory assistance to municipal authorities for airport location, planning, and design, local governments still have the financial burdens of airport construction and improvement. The awakened interest of the states in aeronautics, however, may well make their contribution a substantial element in the matching of some 475 million dollars of Federal grants during the next seven years.

TABLE 2
CLASSIFICATION OF AIRPORTS

Class	Aircraft	Capacity
I	Private-owner smaller type	2- to 5-place aircraft—adequate for aircraft up to 4,000 lb. gross weight; adapted to needs of small communities & auxiliary airports in metropolitan areas; landing strips 1,800 to 2,700 ft. in length.
II	Larger private-owner and smaller transport	Up to 20 place; adequate for aircraft up to 15,000 lb. gross weight; for communities of 5,000 to 25,000 population; runways 2,500 to 3,500 ft. in length.
III	Present-day twin-engine transport	Up to 30 place; adequate for aircraft up to 50,000 lb. gross weight; cities of 25,000 to 250,000 population; runways 3,500 to 4,500 ft. in length.
IV and V	Largest in use and planned for immediate future	30 place and larger; adequate for aircraft of more than 50,000 lb. gross weight; major metropolitan centers and air terminals; Class IV runways 4,500 to 5,500 ft. in length; Class V runways 5,500 ft. in length and over.

SOURCE: Civil Aeronautics Administration, *Civil Aeronautics Journal*, August 15, 1944, p. 100.

Illinois State Surplus and Debt — III

Prospective Use of State Credit

The likelihood that Illinois will use its credit during the early postwar years now appears to depend upon policies adopted with regard to veterans' compensation and upon expenditures for airports, super-highways, and housing. A cash bonus is almost certain to entail borrowing; the expansion and modernization of the highway system, airport development, and public housing may lead to direct or indirect borrowing by the State, but there is a greater probability that pay-as-you-go financing or private and municipal credit will be employed.

Airports—Illinois recently has manifested an interest in aeronautics by creating a separate code department to promote and foster the development of civil aviation. The Post War Public Works Act appropriated 2.5 million dollars in the current biennium for a statewide system of airports to be developed cooperatively with the Federal Government and the municipalities. These funds may be used for airport plans and specifications, for acquisition of land and air rights, and for construction, improvement, repair, and even maintenance of airports or landing areas and their related facilities. It is doubtful, however, that the State will need to use its credit on even a modest scale to aid directly or indirectly in the acquisition of land and the construction of airports. To date, the major governmental outlays for airports have come from the Federal and local governments. The Federal Airport Act, authorizing 500 million dollars in matching Federal aid for airport construction and expansion over a seven-year period, may well affect the State's policy. That Act provides that Federal aid may go directly to local communities unless the state prohibits its political subdivisions from making applications for Federal funds without first channeling them through a state agency or department. It does not necessarily follow that if Illinois were to require this procedure (it does not now do so), the State would incur a financial obligation to match Federal funds. It seems more likely, however, that the State will ultimately assume more direct responsibility for airport financing if the State Department of Aeronautics exercises such authority than if funds are granted directly to participating localities.

Highways—No proposals are current to use State credit directly for highway construction. Some of the counties and cities, however, have evidenced an intention to use their shares of the State motor fuel tax to service bond issues for highway construction.¹ In Cook County, for example, consideration is being given by County and Chicago officials to issues of this type for super-highways totaling 90 million dollars. Large balances in State highway funds, substantial Federal grants-in-aid, and increases in current revenues from highway-user taxes are sufficient to finance an extensive State highway program without resort to borrowing. Furthermore, the developmental era for public roads, during which loans were the only practicable source of funds, is nearly

over. Capital outlays for replacement, modernization, and repair are being met by a well-developed system of highway-user taxes which are or can be made sufficiently productive to cover all reasonable demands for highway facilities.

Housing—The prospect of large-scale State borrowing for housing, even indirectly through the medium of public corporations or trusts, presently seems remote. While the demand for housing indicates a very large investment in that field in the postwar years, both local and private capital appear to be available in sufficient amounts to absorb available material and labor resources. The State's housing program, moreover, is primarily directed at encouraging and facilitating private investment in housing facilities. The State Housing Board operates through the local Housing Authority or Land Clearance Commission to assist local communities with their housing programs and plans. Major emphasis is placed on slum clearance and site acquisition. Although the Board has a 10 million-dollar appropriation for grants to local agencies, it is expected that this sum will be in large measure a revolving fund to facilitate the temporary financing of the cost of sites. Such sites may then be sold or leased to private limited-dividend housing corporations, insurance companies, or local housing authorities that will finance site costs and undertake major construction outlays.

Veterans' Bonus—Proposals for a cash bonus to veterans of World War II are receiving serious consideration. The 64th General Assembly created the Illinois Veterans' Compensation Commission, composed of fifteen members, to study plans of other states, consult with veterans' groups, and develop a plan of compensation and financing suitable to Illinois. The recommendations of this Commission submitted to the Governor on May 15, 1946, include the use of the State's credit to finance the compensation payments. The Governor called the General Assembly into special session on May 24. Any action by the General Assembly involving a State bond issue must be approved by the electorate at a general election. A proposal can first be submitted to the voters in November 1946 and next in November 1948. The referendum must include a financial plan covering interest charges and amortization of the debt.

The Commission report recommends payments of \$10 per month for service in the United States and \$15 per month for service overseas. A minimum payment of \$50 for sixty days' service and a flat amount of \$900 to the next of kin of military personnel who have lost their lives in the service are also provided. The total cost is estimated at 385 million dollars, including approximately 25 million dollars for administrative expenses. The number of veterans eligible for benefits is estimated at 916,000. On the basis of these totals, the average actual payment to veterans would be about \$400, and the average cost of administration approximately \$20.

The bonus, if financed entirely by borrowing, would increase the State's outstanding debt to nearly four and one-half times its present level. The relative significance of the magnitude of such an issue is evident from the fact that a 385 million-dollar loan would be equivalent to one-fourth of the net long-term debt now outstanding for all of the forty-eight states.

Following World War I, seventeen states issued bonds aggregating 337 million dollars for veterans' cash bonuses. One of these states and two others incurred indebtedness totaling 107 million dollars to establish loan funds for financing veterans' purchases of homes and farms. Three states financed cash bonuses out of current tax receipts and some short-term borrowing. In six states projected bond issues were either rejected by referendum or the courts and, in one instance, by a governor's veto. Nearly all bonus proposals were first considered at legislative sessions in 1919, 1920, or 1921. Due to constitutional, referendum, and other complications, however, some bonuses were not paid until several years later, e.g., New York in 1924 and Pennsylvania in 1934.

The states paying cash bonuses were concentrated in the East (Maine, Massachusetts, New Hampshire, New Jersey, New York, Pennsylvania, Rhode Island, and Vermont), the Middle West (Illinois, Iowa, Kansas, Michigan, Missouri, Minnesota, North Dakota, Ohio, South Dakota, and Wisconsin), and the Pacific Coast (Oregon and Washington). In the Seventh District, Illinois issued bonds aggregating 55 million dollars; Iowa, 22 million dollars; and Michigan, 25 million dollars. The bonus proposal in Indiana was vetoed by the Governor, and in Wisconsin tax collections totaling over 22 million dollars were used for a cash bonus and educational aids.²

World War II bonuses have already been authorized in Massachusetts, New Hampshire, Rhode Island, and Vermont. New York initiated a bonus plan by enacting a law in March 1946 authorizing a 400 million-dollar bond issue. The measure must be re-enacted by the 1947 legislature before it is submitted to a vote of the people in the fall of 1947. The New Hampshire bonus, authorized in 1943, provides payments of \$10 per month of service with a maximum of \$100. It is estimated to cost 5 million dollars. A poll tax for a two-year period provides a portion of the revenue; the balance is to be financed by a 3.6 million-dollar bond issue. The Vermont bonus is similar except that it affords a maximum of \$120. The cost is estimated at between 3.5 and 4.0 million dollars and will be paid from a treasury surplus. The Massachusetts plan, enacted in 1945, provides a flat \$100 payment which will aggregate between 60 and 70 million dollars, and is to be financed on a current and short-term loan basis by the enactment of additional taxes on liquor, cigarettes, and corporations. A liberalization of the Massachusetts payments is now being considered by the General Court; it is proposed that veterans with overseas service receive an additional \$200 and those with service in the United States an additional \$100. The Rhode Island bonus is a flat sum of \$200 to each veteran and merchant seaman. Two bond issues are to be submitted to the voters in November: one for veterans of 19.5 million dollars and

one for merchant seamen of .5 million dollars.

The New York bonus provides \$50 for less than sixty days' service, \$150 for more than sixty days in the United States, and \$250 for service abroad. It is estimated that 1,700,000 persons will qualify for benefits, with 3 per cent in the first category, 22 per cent in the second, and 75 per cent in the third.

In addition to these five states in which bonus proposals have been crystallized and received legislative approval, several states have set aside treasury surpluses for veterans' benefits, e. g., Michigan and Wisconsin have postwar funds earmarked for veterans of 50 million dollars and 7 million dollars respectively. In some states such reserves no doubt will be used for cash bonuses with or without supplementary borrowing.

The specific bonus plans for World War II veterans follow rather closely the precedents established after World War I in scale of benefits, timing, and financial arrangements, thus indicating that the pattern and scope of payments is likely to compare with that following the first World War after allowance is made for a threefold increase in number of eligibles.

²Such issues, however, will carry the pledge of property tax revenues if other sources of income are inadequate. The probability that some future General Assembly will decrease city or county shares of highway-user taxes may be remote, despite the fact that during the 1930's the emergency relief bonds were serviced by such a diversion. Short of a constitutional amendment, there seems to be no way in which these revenues can be irrevocably pledged to the localities. The 61st General Assembly (1939) in Senate Bill 184 directed certain State officials to issue notes, payable from Cook County's and the City of Chicago's share of the motor fuel tax funds accruing after June 30, 1939, and before June 30, 1959. The proceeds of these notes were to be used for highway and street improvements by Chicago and by Cook County in the proportion that their allotments of fuel tax revenues were encumbered. In the suit testing the constitutionality of this act, it was contended that the notes were not in the nature of anticipation warrants but rather that they were obligations secured by a pledge of motor fuel taxes, which in reality were service charges or tolls for the use of the highways and that these earnings could be earmarked for debt service without infringing on any constitutional restriction. The act stated: "Said notes are issued under the provision of this Act and do not constitute an indebtedness of the state or of the county or municipality within any constitutional limitation." Rejecting this contention and holding the act unconstitutional in *People vs. Barrett*, 373 Ill. 393, April 10, 1940, the court said:

"The special fund doctrine, which, in cases of water and electric light utilities and bridge tolls, constitute an exception to the debt-limitation provision, is based on the theory that an obligation incurred in the acquisition, construction or extension of income-bearing property and payable solely from the income of that property, is not a debt of the State or municipality. Such doctrine does not, in our opinion, extend to obligations payable from taxes, which, in whatever form the legislature may collect them, are State revenues. As we have seen, the limitation by the constitution of this State upon the creation of debts by the State, includes not only debts payable from a tax on property but also debts payable 'from other sources of revenue.'

"... the General Assembly may transfer motor fuel tax funds from one use to another, where that fund has not already been pledged to the payment of bonds theretofore issued in accordance with the provisions of the constitution. Such funds are revenues of the State, and the General Assembly, subject to that limitation, is empowered to subdivide them into any funds it sees fit, or remove them from one fund to another.

"... By attempting to control the maintenance of the tax rate on gasoline, and, by its obligation under the act, to attempt to maintain the amount and proportion of the tax raised which shall be paid to the city for whose benefit the notes are issued, the legislature has thus attempted to make the State responsible for the payment of those notes and they become, therefore, the debts of the State. We are of the opinion that Senate Bill No. 184 creates a debt against the State contrary to constitutional limitations.

"... It is fundamental, under our constitution, that the Legislature possesses every power not delegated to some other department or to the federal government, or not denied to it by the Constitution of the state or of the United States. . . . this court [has] held that the General Assembly has the undoubted right to repeal all legislative acts which are not in the nature of a private grant . . . [and] that it is not competent for the legislature to attempt to limit its own legislative powers. Under section 18 of article 4 of the constitution the pledging of funds for the payment of bonds and interest is permitted when it is done in the manner set forth, that is, by the approval of the vote of the people at a general election. Wanting such vote in this case, the General Assembly is without power to delegate to the executive department the power, by the issuance of notes, to pledge the motor fuel tax fund for the retirement of those notes over a period of years, so as to prevent succeeding General Assemblies from repealing the Motor Fuel Tax Law entirely, reducing the rate, or changing the purposes or fund into which it is to be paid. . . ."

²Ratchford, B. U., *American State Debts*, pp. 313-32.

SEVENTH FEDERAL



RESERVE DISTRICT



